

section, a taxpayer cannot adopt or retain a taxable year under this section unless the return or form required to effect or request the adoption or retention is filed by its due date (with extensions if the adoption is effected by filing an income tax return for the taxpayer's first taxable year).

(2) A taxpayer may adopt or retain a taxable year under this section if the due date (without regard to extensions) for the return or form required to effect or request the adoption or retention is on or after November 6, 1986, and before March 9, 1987, and the return or form is filed before March 9, 1987 (or, in the case of an adoption effected by filing an income tax return for the taxpayer's first taxable year, if an application for extension is filed before March 9, 1987). This paragraph (d)(2) only extends the time for adopting or retaining a taxable year and does not extend the time for making an S election. An S election that is timely filed before March 9, 1987, however, will not be denied or rendered ineffective solely by reason of the need for the taxpayer to submit the information required by paragraph (c) of this section.

(3) In the case of an adoption or retention of a taxable year under this section that is effected by filing an income tax return for the taxpayer's first taxable year, any failure to file a return or to pay tax on or before the due date for the return or the date prescribed for payment will be treated as due to reasonable cause and will not give rise to any addition to tax under section 6651 if—

(i) The due date for the return (without regard to extensions) or the date prescribed for payment is on or after November 6, 1986, and before March 9, 1987, and

(ii) The return (or application for extension) is filed and the tax is paid before March 9, 1987.

(e) *Effective date.* This section generally applies if the first taxable year of the partnership or the first taxable year for which the election to be an S corporation is effective begins before January 1, 1987, unless the application necessary to effect or request the adoption or retention was timely filed before November 6, 1986. This section shall not apply, however, to an adop-

tion by a partnership of a taxable year that begins before January 1, 1986.

[T.D. 8123, 52 FR 3622, Feb. 5, 1987]

§ 1.443-1 Returns for periods of less than 12 months.

(a) *Returns for short period.* A return for a short period, that is, for a taxable year consisting of a period of less than 12 months, shall be made under any of the following circumstances:

(1) *Change of annual accounting period.* In the case of a change in the annual accounting period of a taxpayer, a separate return must be filed for the short period of less than 12 months beginning with the day following the close of the old taxable year and ending with the day preceding the first day of the new taxable year. However, such a return is not required for a short period of six days or less, or 359 days or more, resulting from a change from or to a 52-53-week taxable year. See section 441(f) and § 1.441-2. The computation of the tax for a short period required to effect a change of annual accounting period is described in paragraph (b) of this section. In general, a return for a short period resulting from a change of annual accounting period shall be filed and the tax paid within the time prescribed for filing a return for a taxday of the short period. For rules applicable to a subsidiary corporation which becomes a member of an affiliated group which files a consolidated return, see § 1.1502-76.

(2) *Taxpayer not in existence for entire taxable year.* If a taxpayer is not in existence for the entire taxable year, a return is required for the short period during which the taxpayer was in existence. For example, a corporation organized on August 1 and adopting the calendar year as its annual accounting period is required to file a return for the short period from August 1 to December 31, and returns for each calendar year thereafter. Similarly, a dissolving corporation which files its returns for the calendar year is required to file a return for the short period from January 1 to the date it goes out of existence. Income for the short period is not required to be annualized if the taxpayer is not in existence for the entire

taxable year, and, in the case of a taxpayer other than a corporation, the deduction under section 151 for personal exemptions (or deductions in lieu thereof) need not be reduced under section 443(c). In general, the requirements with respect to the filing of returns and the payment of tax for a short period where the taxpayer has not been in existence for the entire taxable year are the same as for the filing of a return and the payment of tax for a taxable year of 12 months ending on the last day of the short period. Although the return of a decedent is a return for the short period beginning with the first day of his last taxable year and ending with the date of his death, the filing of a return and the payment of tax for a decedent may be made as though the decedent had lived throughout his last taxable year.

(b) *Computation of tax for short period on change of annual accounting period—*

(1) *General rule.* (i) If a return is made for a short period resulting from a change of annual accounting period, the taxable income for the short period shall be placed on an annual basis by multiplying such income by 12 and dividing the result by the number of months in the short period. Unless section 443(b)(2) and subparagraph (2) of this paragraph apply, the tax for the short period shall be the same part of the tax computed on the annual basis as the number of months in the short period is of 12 months.

(ii) If a return is made for a short period of more than 6 days, but less than 359 days, resulting from a change from or to a 52-53-week taxable year, the taxable income for the short period shall be annualized and the tax computed on a daily basis, as provided in section 441(f)(2)(B)(iii) and paragraph (c)(5) of § 1.441-2.

(iii) For method of computation of income for a short period in the case of a subsidiary corporation required to change its annual accounting period to conform to that of its parent, see § 1.1502-76(b).

(iv) An individual taxpayer making a return for a short period resulting from a change of annual accounting period is not allowed to take the standard deduction provided in section 141 in com-

puting his taxable income for the short period. See section 142(b)(3).

(v) In computing the taxable income of a taxpayer other than a corporation for a short period (which income is to be annualized in order to determine the tax under section 443(b)(1)) the personal exemptions allowed individuals under section 151 (and any deductions allowed other taxpayers in lieu thereof, such as the deduction under section 642(b)) shall be reduced to an amount which bears the same ratio to the full amount of the exemptions as the number of months in the short period bears to 12. In the case of the taxable income for a short period resulting from a change from or to a 52-53-week taxable year to which section 441(f)(2)(B)(iii) applies, the computation required by the preceding sentence shall be made on a daily basis, that is, the deduction for personal exemptions (or any deduction in lieu thereof) shall be reduced to an amount which bears the same ratio to the full deduction as the number of days in the short period bears to 365.

(vi) If the amount of a credit against the tax (for example, the credits allowable under section 34 (for dividends received on or before December 31, 1964), and 35 (for partially tax-exempt interest)) is dependent upon the amount of any item of income or deduction, such credit shall be computed upon the amount of the item annualized separately in accordance with the foregoing rules. The credit so computed shall be treated as a credit against the tax computed on the basis of the annualized taxable income. In any case in which a limitation on the amount of a credit is based upon taxable income, taxable income shall mean the taxable income computed on the annualized basis.

(vii) The provisions of this subparagraph may be illustrated by the following examples:

Example (1). A taxpayer with one dependent who has been granted permission under section 442 to change his annual accounting period files a return for the short period of 10 months ending October 31, 1956. He has income and deductions as follows:

Income			
Interest income	\$10,000.00
Partially tax-exempt interest with respect to which a credit is allowable under section 35	500.00

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Dividends to which sections 34 and 116 are applicable	750.00	
		11,250.00
<i>Deductions</i>		
Real estate taxes	200.00	
2 personal exemptions at \$600 on an annual basis	1,200.00	
The tax for the 10-month period is computed as follows:		
Total income as above ..	11,250.00	
Less:		
Exclusion for dividends received	\$50.00	
2 personal exemptions (\$1,200× ¹⁰ / ₁₂)	1,000.00	
Real estate taxes	200.00	
		1,250.00
Taxable income for 10-month period before annualizing		10,000.00
Taxable income annualized (10,000× ¹² / ₁₀)		12,000.00
Tax on \$12,000 before credits		3,400.00
Deduct credits:		
Dividends received for 10-month period	\$750.00	
Less: Excluded portion	50.00	
Included in gross income	700.00	
Dividend income annualized (\$700× ¹² / ₁₀)	840.00	
Credit (4 percent of \$840)		33.60
Partially tax-exempt interest included in gross income for 10-month period	500.00	
Partially tax-exempt interest (annualized) (\$500× ¹² / ₁₀)	600.00	
Credit (3 percent of \$600)		18.00
		51.60
Tax on \$12,000 (after credits)		3,348.40
Tax for 10-month period (\$3,348.40× ¹⁰ / ₁₂)		2,790.33

Example (2). The X Corporation makes a return for the one-month period ending September 30, 1956, because of a change in annual accounting period permitted under section 442. Income and expenses for the short period are as follows:

Gross operating income	\$126,000
Business expenses	130,000
Net loss from operations	(4,000)
Dividends received from taxable domestic corporations	30,000
Gross income for short period before annualizing	26,000

Dividends received deduction (85 percent of \$30,000, but not in excess of 85 percent of \$26,000)	22,100
Taxable income for short period before annualizing	3,900
Taxable income annualized (\$8,900× ¹² / ₁₂)	46,800
Tax on annual basis:	
\$46,800 at 52 percent	\$24,336
Less surtax exemption	5,500
	\$18,836
Tax for 1-month period (\$18,836× ¹ / ₁₂)	1,570

Example (3). The Y Corporation makes a return for the six-month period ending June 30, 1957, because of a change in annual accounting period permitted under section 442. Income for the short period is as follows:

Taxable income exclusive of net long-term capital gain	\$40,000
Net long-term capital gain	10,000
Taxable income for short period before annualizing	50,000
Taxable income annualized (\$50,000× ¹² / ₆)	100,000

Regular tax computation

Taxable income annualized	100,000
Tax on annual basis:	
\$100,000 at 52 percent	\$52,000
Less surtax exemption	5,500
	46,500
Tax for 6-month period (\$46,500× ⁶ / ₁₂)	23,250

Alternative tax computation

Taxable income annualized	100,000
Less annualized capital gain (\$10,000× ¹² / ₆)	20,000
Annualized taxable income subject to partial tax	80,000

Partial tax on annual basis

\$60,000 at 52 percent	\$41,600
Less surtax exemption	5,500
	36,100
25 percent of annualized capital gain (\$20,000) ...	5,000
Alternative tax on annual basis	41,100
Alternative tax for 6-month period (\$41,100× ⁶ / ₁₂)	20,550

Since the alternative tax of \$20,550 is less than the tax computed in the regular manner (\$23,250), the corporation's tax for the 6-month short period is \$20,550.

(2) *Exception: computation based on 12-month period.* (i) A taxpayer whose tax would otherwise be computed under section 443(b)(1) (or section 441(f)(2)(B)(iii) in the case of certain changes from or to a 52-53-week taxable year) for the short period resulting from a change of annual accounting period may apply to the district director to have his tax computed under the provisions of section 443(b)(2) and this subparagraph. If such application is made, as provided in subdivision (v) of

this subparagraph, and if the taxpayer establishes the amount of his taxable income for the 12-month period described in subdivision (ii) of this subparagraph, then the tax for the short period shall be the greater of the following—

(a) An amount which bears the same ratio to the tax computed on the taxable income which the taxpayer has established for the 12-month period as the taxable income computed on the basis of the short period bears to the taxable income for such 12-month period; or

(b) The tax computed on the taxable income for the short period without placing the taxable income on an annual basis.

However, if the tax computed under section 443(b)(2) and this subparagraph is not less than the tax for the short period computed under section 443(b)(1) (or section 441(f)(2)(B)(iii) in the case of certain changes from or to a 52-53-week taxable year), then section 443(b)(2) and this subparagraph do not apply.

(ii) The term “12-month period” referred to in subdivision (i) of this subparagraph means the 12-month period beginning on the first day of the short period. However, if the taxpayer is not in existence at the end of such 12-month period, or if the taxpayer is a corporation which has disposed of substantially all of its assets before the end of such 12-month period, the term “12-month period” means the 12-month period ending at the close of the last day of the short period. For the purposes of the preceding sentence, a corporation which has ceased business and distributed so much of the assets used in its business that it cannot resume its customary operations with the remaining assets, will be considered to have disposed of substantially all of its assets. In the case of a change from a 52-53-week taxable year, the term “12-month period” means the period of 52 or 53 weeks (depending on the taxpayer’s 52-53-week taxable year) beginning on the first day of the short period.

(iii)(a) The taxable income for the 12-month period is computed under the same provisions of law as are applicable to the short period and is computed as if the 12-month period were an ac-

tual annual accounting period of the taxpayer. All items which fall in such 12-month period must be included even if they are extraordinary in amount or of an unusual nature. If the taxpayer is a member of a partnership, his taxable income for the 12-month period shall include his distributive share of partnership income for any taxable year of the partnership ending within or with such 12-month period, but no amount shall be included with respect to a taxable year of the partnership ending before or after such 12-month period. If any other item partially applicable to such 12-month period can be determined only at the end of a taxable year which includes only part of the 12-month period, the taxpayer, subject to review by the Commissioner, shall apportion such item to the 12-month period in such manner as will most clearly reflect income for the 12-month period.

(b) In the case of a taxpayer permitted or required to use inventories, the cost of goods sold during a part of the 12-month period included in a taxable year shall be considered, unless a more exact determination is available, as such part of the cost of goods sold during the entire taxable year as the gross receipts from sales for such part of the 12-month period is of the gross receipts from sales for the entire taxable year. For example, the 12-month period of a corporation engaged in the sale of merchandise, which has a short period from January 1, 1956, to September 30, 1956, is the calendar year 1956. The three-month period, October 1, 1956, to December 31, 1956, is part of the taxpayer’s taxable year ending September 30, 1957. The cost of goods sold during the three-month period, October 1, 1956, to December 31, 1956, is such part of the cost of goods sold during the entire fiscal year ending September 30, 1957, as the gross receipts from sales for such three-month period are of the gross receipts from sales for the entire fiscal year.

(c) The Commissioner may, in granting permission to a taxpayer to change his annual accounting period, require, as a condition to permitting the change, that the taxpayer must take a closing inventory upon the last day of

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the 12-month period if he wishes to obtain the benefits of section 443(b)(2). Such closing inventory will be used only for the purposes of section 443(b)(2), and the taxpayer will not be required to use such inventory in computing the taxable income for the taxable year in which such inventory is taken.

(iv) The provisions of this subparagraph may be illustrated by the following examples:

Example (1). The taxpayer in example (1) under paragraph (b)(1)(vii) of this section establishes his taxable income for the 12-month period from January 1, 1956, to December 31, 1956. The taxpayer has a short period of 10 months, from January 1, 1956, to October 31, 1956. The taxpayer files an application in accordance with subdivision (v) of this subparagraph to compute his tax under section 443(b)(2). The taxpayer's income and deductions for the 12-month period, as so established, follow:

Income	
Interest income	\$11,000
Partially tax-exempt interest with respect to which a credit is allowable under section 35	600
Dividends to which sections 34 and 116 are applicable	850
	12,450
Deductions	
Real estate taxes	200
2 personal exemptions at \$600	1,200
<i>Tax computation for short period under section 443(b)(2)(A)(i)</i>	
Total income as above	\$12,450
Less:	
Exclusion for dividends received	\$50
Personal exemptions	1,200
Deduction for taxes	200
	1,450
Taxable income for 12-month period	11,000
Tax before credits	3,020
Credit for partially tax-exempt interest (3 percent of \$600)	18
Credit for dividends received (4 percent of (\$850 - 50))	32
	50
Tax under section 443(b)(2)(A)(i) for 12-month period	2,970
Taxable income for 10-month short period from example (1) of paragraph (b)(1)(vii) of this section before annualizing	10,000
Tax for short period under section 443(b)(2)(A)(i) (\$2,970 × \$10,000 (taxable income for short period) / \$11,000 (taxable income for 12-month period))	2,700
<i>Tax computation for short period under section 443(b)(2)(A)(ii)</i>	
Total income for 10-month short period	11,250

Less:	
Exclusion for dividends received	50
2 personal exemptions	1,200
Real estate taxes	200
	1,450
Taxable income for short period without annualizing and without proration of personal exemptions	9,800
Tax before credits	2,572
Less credits:	
Partially tax-exempt interest (3 percent of \$500)	15
Dividends received (4 percent of (\$750 - 50))	28
	43
Tax for short period under section 443(b)(2)(A)(ii)	2,529

The tax of \$2,700 computed under section 443(b)(2)(A)(i) is greater than the tax of \$2,529, computed under section 443(b)(2)(A)(ii), and is, therefore, the tax under section 443(b)(2). Since the tax of \$2,700 (computed under section 443(b)(2)) is less than the tax of \$2,790.33 (computed under section 443(b)(1)) on the annualized income of the short period (see example (1) of paragraph (b)(1)(vii) of this section), the taxpayer's tax for the 10-month short period is \$2,700.

Example (2). Assume the same facts as in example (1) of this subdivision, except that, during the month of November 1956, the taxpayer suffered a casualty loss of \$5,000. The tax computation for the short period under section 443(b)(2) would be as follows:

<i>Tax computation for short period under section 443(b)(2)(A)(i)</i>	
Taxable income for 12-month period from example (1)	\$11,000
Less: Casualty loss	5,000
Taxable income for 12-month period	6,000
Tax before credits	\$1,360
Credits from example (1)	50
Tax under section 443(b)(2)(A)(i) for 12-month period	1,310
Tax for short period (\$1,310 × \$10,000 / \$6,000) under section 443(b)(2)(A)(i)	2,183
<i>Tax computation for short period under section 443(b)(2)(A)(ii)</i>	
Total income for the short period	11,250
Less:	
Exclusion for dividends received	50
2 personal exemptions	1,200
Real estate taxes	200
	1,450
Taxable income for short period without annualizing and without proration of personal exemptions	9,800
Tax before credits	2,572
Less credits:	
Partially tax-exempt interest (3 percent of \$500)	15

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Dividends received (4 percent of \$750 - 50))	28
	43
Tax for short period under section 443(b)(2)(A)(ii)	2,529

The tax of \$2,529, computed under section 443(b)(2)(A)(ii) is greater than the tax of \$2,183 computed under section 443(b)(2)-(A)(i) and is, therefore, the tax under section 443(b)(2). Since this tax is less than the tax of \$2,790.33, computed under section 443(b)(1) (see example (1) of paragraph (b)(1)(vii) of this section), the taxpayer's tax for the 10-month short period is \$2,529.

(v)(a) A taxpayer who wishes to compute his tax for a short period resulting from a change of annual accounting period under section 443(b)(2) must make an application therefor. Except as provided in (b) of this subdivision, the taxpayer shall first file his return for the short period and compute his tax under section 443(b)(1). The application for the benefits of section 443(b)(2) shall subsequently be made in the form of a claim for credit or refund. The claim shall set forth the computation of the taxable income and the tax thereon for the 12-month period and must be filed not later than the time (including extensions) prescribed for filing the return for the taxpayer's first taxable year which ends on or after the day which is 12 months after the beginning of the short period. For example, assume that a taxpayer changes his annual accounting period from the calendar year to a fiscal year ending September 30, and files a return for the short period from January 1, 1956, to September 30, 1956. His application for the benefits of section 443(b)(2) must be filed not later than the time prescribed for filing his return for his first taxable year which ends on or after the last day of December 1956, the twelfth month after the beginning of the short period. Thus, the taxpayer must file his application not later than the time prescribed for filing the return for his fiscal year ending September 30, 1957. If he obtains an extension of time for filing the return for such fiscal year, he may file his application during the period of such extension. If the district director determines that the taxpayer has established the amount of his taxable income for the 12-month period, any excess of the tax paid for the short

period over the tax computed under section 443(b)(2) will be credited or refunded to the taxpayer in the same manner as in the case of an overpayment.

(b) If at the time the return for the short period is filed, the taxpayer is able to determine that the 12-month period ending with the close of the short period (see section 443(b)(2)-(B)(ii) and subparagraph (2)(ii) of this paragraph) will be used in the computations under section 443(b)(2), then the tax on the return for the short period may be determined under the provisions of section 443(b)(2). In such case, a return covering the 12-month period shall be attached to the return for the short period as a part thereof, and the return and attachment will then be considered as an application for the benefits of section 443(b)(2).

(c) *Adjustment in deduction for personal exemption.* For adjustment in the deduction for personal exemptions in computing the tax for a short period resulting from a change of annual accounting period under section 443(b)(1) (or under section 441(f)(2)(B)(iii) in the case of certain changes from or to a 52-53-week taxable year), see paragraph (b)(1)(v) of this section.

(d) *Adjustments in exclusion of computing minimum tax for tax preferences.*

(1) If a return is made for a short period on account of any of the reasons specified in subsection (a) of section 443, the \$30,000 amount specified in section 56 (relating to minimum tax for tax preferences), modified as provided by section 58 and the regulations thereunder, shall be reduced to the amount which bears the same ratio to such specified amount as the number of days in the short period bears to 365.

(2) *Example.* The provisions of this paragraph may be illustrated by the following example:

Example. A taxpayer who is an unmarried individual has been granted permission under section 442 to change his annual accounting period files a return for the short period of 4 months ending April 30, 1970. The \$30,000 amount specified in section 56 is reduced as follows:

$$(120/365) \times \$30,000 = \$9,835.89.$$

(e) *Cross references.* For inapplicability of section 443(b) and paragraph (b) of this section in computing—

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(1) Accumulated earnings tax, see section 536 and the regulations thereunder;

(2) Personal holding company tax, see section 546 and the regulations thereunder;

(3) Undistributed foreign personal holding company income, see section 557 and the regulations thereunder;

(4) The taxable income of a regulated investment company, see section 852(b)(2)(E) and the regulations thereunder; and

(5) The taxable income of a real estate investment trust, see section 857(b)(2)(C) and the regulations thereunder.

[T.D. 6500, 25 F.R. 11705, Nov. 26, 1960, as amended by T.D. 6598, 27 FR 4093, Apr. 28, 1962; T.D. 6777, 29 FR 17808, Dec. 16, 1964; T.D. 7244, 37 FR 28897, Dec. 30, 1972, T.D. 7564, 43 FR 40494, Sept. 12, 1978; T.D. 7575, 43 FR 58816, Dec. 18, 1978; T.D. 7767, 465 FR 11265, Feb. 6, 1981]

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